

**DRAFT**

**REPORT OF INVESTIGATION INTO  
UNAUTHORIZED USE OF  
APPROPRIATED FUNDS FOR FIXED  
CAPITAL OUTLAY PROJECTS AT THE  
UNIVERSITY OF CENTRAL FLORIDA**

**Distributed March 11, 2019**

**Public Integrity & Ethics Committee  
Florida House of Representatives  
Rep. Thomas J. Leek, Chair**

## **I. Executive Summary of Report**

Legislative oversight is the broad responsibility of elected representatives to review, monitor, and supervise the implementation of public policy and the use of public funds. This function provides an essential check and balance among the branches of government. Legislative oversight is also essential to the responsible and effective appropriation of state funds. Investigations of possible violations of state law regarding the use of public funds are necessary for the integrity of government and accountability to the taxpayers.

Speaker Richard Corcoran initiated the House investigation into the University of Central Florida capital outlays in September 2018, as a result of findings by the Auditor General that UCF used Education and General (“E&G”) carryforward funds for construction of a new academic building in violation of s. 216.292(5), Florida Statutes and Board of Governors Regulation 9.007. Responsibility for the investigation was delegated to the Public Integrity and Ethics Committee.

This report presents background information and describes the investigation conducted by the Committee between September 2018 and March 2019. The investigative process included review of an extensive record of financial transactions and meetings by the staff and governing boards. In addition, interviews were conducted with key personnel, culminating in sworn testimony by thirteen individuals subpoenaed by the Committee. One individual, former UCF president John Hitt, is notable for his limited participation.

The Committee’s key findings are as follows:

1. UCF improperly transferred as much as \$85 million of E&G carryforward funds to university construction accounts for unauthorized uses.
2. UCF administrators failed to timely disclose improper fund transfers when discovered.
3. UCF administrators’ response to the audit finding confounded a careful review of some questioned transfers.
4. UCF’s budgeting and spending practices fostered ad hoc and unaccountable decisions.
5. Significant deficiencies exist in the capital budgeting and planning process of UCF.
6. Compliance activities of the university were inadequate to identify the misspending.
7. UCF BOT lacked training and information necessary to fulfill their fiduciary responsibilities.
8. Allocation of unrealized investment gains is an inappropriate means to fund operations.
9. Limited oversight by the Board of Governors contributed to UCF misspending.
10. BOG Inspector General lacks resources for robust oversight.

As a result of its investigation, the Committee recommends:

- Strict adherence to planning and budget laws and regulations;
- Establishment of sufficient checks and balances to prevent one or a few administrators from controlling both information and authority;
- Additional training for BOT members;
- Reform of certain BOG regulations and practices;
- Development of BOT policies and procedures to provide better internal controls; and
- Additional investigation by the BOG of complaints of waste, fraud and mismanagement.

## **II. Background**

### **A. Audit**

The Auditor General conducted an operational audit of UCF from March through September 2018. On August 7, auditors informed UCF administrators of likely findings including the misuse of E&G carryforward funds for construction of a new academic building in violation of BOG Reg. 9.007. Shortly thereafter, auditors contacted Board of Governors (“BOG”) staff for clarification on the application of BOG Reg. 9.007 to the use of E&G carryforward funds for construction of Trevor Colbourn Hall (“TCH”).

On November 27, 2018, the Auditor provided the preliminary and tentative findings of its audit to UCF. In pertinent part, the Auditor found that:

- UCF used E&G carryforward funds to construct TCH;
- UCF misreported the funding source in annual capital outlay budgets of the past four years by listing the TCH project under the category of Projects Funded by PECO;
- UCF misreported the Colbourn Hall and TCH projects as deferred maintenance projects and did not identify the projects by name in annual Operating Budget – Beginning Carryforward Fund Balance Composition Reports (“Fund Composition Reports”) submitted to the BOG during a five-year period,;
- UCF used \$16,910,886 of unrealized investment gains to replenish E&G carryforward funds expended on construction projects; and
- In addition to the TCH funding, UCF had transferred \$46.5 million of E&G carryforward funds for 11 other construction projects, including \$13.8 million that had been spent as of September 18, 2018, and \$32.7 million that had not yet been spent.

### **B. BOG Preliminary Review**

In August 2018, BOG Chancellor Marshall Criser contacted UCF regarding the audit finding. UCF reported on the matter at a September 13, 2018 BOG meeting. On September 14, BOG Chair Ned

C. Lautenbach reported the matter to the Governor and Legislature as a serious breach of trust and advising of actions the BOG intended to take in response. The BOG assigned its Inspector General to work with the Auditor General’s office on resolution of the matter.

#### C. Bryan Cave Investigation

On September 20, 2018, UCF Board of Trustees (“BOT”) approved retention of Atlanta law firm Bryan Cave Leighton Paisner (“Bryan Cave”) to investigate the use of E&G funds for capital projects. Bryan Cave was directed to investigate five questions:

- Was anyone besides the former CFO, William Merck, involved in the decisions to use E&G funds for capital projects?
- Did anyone personally profit from these decisions?
- Were there additional capital projects beyond those identified to date in which E&G funds were improperly utilized?<sup>1</sup>
- Were there internal controls that failed to prevent or detect this activity or that were violated?
- What additional controls should be put in place to ensure that this does not happen again at UCF?

Bryan Cave issued its final report on January 17, 2019. The report concluded that former UCF CFO William Merck was the principal figure in all of the decisions to use E&G funds for the construction of TCH.<sup>2</sup> Four of Merck’s subordinates and former Provost Tony Waldrop were identified as having been involved in decisions or key tasks relating to funding the project.<sup>3</sup> The report concluded that former UCF President John C. Hitt was advised in advance of the possibility that the funding for TCH might lead to an adverse audit finding and he directed Merck to go forward with the project anyway.<sup>4</sup> The report determined that former Provost Dale Whittaker received vague and arguably misleading information about the source of funding and was not familiar with restrictions on the use of E&G; however, Whittaker acknowledged that he was aware that the funding source might draw an adverse audit finding.<sup>5</sup> The report found Trustees had been misled about the funding source and were uninformed of the risks or the restrictions on E&G

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<sup>1</sup> The report indicates the scope of the investigation was subsequently narrowed to focus exclusively on TCH excluding other projects for which E&G funds may have been committed or expended. See BC Report at 1. The report may be found at <https://www.ucf.edu/transparency/board-of-trustees-investigation/>.

<sup>2</sup> BC Report at 6.

<sup>3</sup> BC Report at 8-9.

<sup>4</sup> BC Report at 11.

<sup>5</sup> BC Report at 10.

funds.<sup>6</sup> The report also concluded that investigators found no evidence that any UCF employee personally profited from the decision to use E&G funds.<sup>7</sup>

Investigators found deficiencies in UCF's written policies and procedures regarding the use of state appropriated funds, training and education on such policies and applicable laws and regulations, oversight and approval of significant decisions involving the use of appropriated funds, auditing for proper funding of capital projects, monitoring and reporting. Finally, investigators found that UCF failed to foster a culture that encouraged employees to challenge senior members of the administration or reporting illegitimate activity.<sup>8</sup>

#### D. Initiation of House Investigation

On September 14, 2018, Speaker Corcoran wrote UCF President Dale Whittaker to express his concerns and to notify UCF that the House Public Integrity & Ethics Committee ("PIE") would be undertaking an investigation of the matter.

Part V of this report describes the Committee's investigation in more detail.

### **III. Historical and Institutional Context**

#### A. State University System

Florida's State University System ("SUS") includes twelve universities with an enrollment of more than 300,000 students and more than 60,000 faculty and staff.<sup>9</sup> The System has an annual operating budget of approximately \$14.9 billion in revenues including total state appropriations for FY 2018-19 in excess of \$5 billion.<sup>10</sup>

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<sup>6</sup> BC Report at 26, 32-35.

<sup>7</sup> BC Report at 11.

<sup>8</sup> Id.

<sup>9</sup> Statistical information about the SUS was accessed on the BOG website at: <https://www.flbog.edu/universities/>.

<sup>10</sup> State University System of Florida Operating Budget Summary Fiscal Year 2018-2019, p. 12. The SUS Operating Budget can be found on the BOG website at: [https://www.flbog.edu/board/office/budget/docs/2018-19\\_Combined-Final-Book.pdf](https://www.flbog.edu/board/office/budget/docs/2018-19_Combined-Final-Book.pdf). State appropriations include approximately \$2.8 billion general revenue, \$1.8 billion tuition and fees and over \$300 million in lottery funds.

## **B. SUS Governance**

The BOG operates, regulates, controls, and has full responsibility for the management of the state university system.<sup>11</sup> The BOG exercises both legislative and executive powers,<sup>12</sup> subject to the powers of the Legislature to appropriate for the expenditure of funds.<sup>13</sup> Accordingly, the BOG adopts regulations and exercises oversight functions to ensure the faithful execution of the regulations,<sup>14</sup> laws, and constitutional provisions governing the universities. The BOG employs a Chancellor to aid the BOG in the implementation of its responsibilities.<sup>15</sup> The BOG also employs an Inspector General to promote accountability, efficiency, and effectiveness, and to detect fraud and abuse within the universities.<sup>16</sup>

Separate from the BOG, a BOT administers each state university. The BOG establishes the powers and duties of the BOTs.<sup>17</sup> The BOT is responsible for the direction, operation, management and accountability of the university including administration, strategic planning, financial management, personnel policy, property management, academic programs and student affairs, and internal auditing.<sup>18</sup> Each BOT has various reporting responsibilities including submission of budgets and reporting expenditures to the BOG.<sup>19</sup> In the exercise of its responsibilities, each BOT has authority to adopt university regulations.<sup>20</sup>

## **C. Funding and Sources**

University operating budgets are funded by E&G funds including general appropriations, tuition and fees, and state lottery funds. To discourage unnecessary spending, universities are allowed to retain unspent E&G funds left over at the end of a fiscal year.<sup>21</sup> These funds are referred to as E&G

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<sup>11</sup> Fla. Const., Art. IX, s. 7. The BOG has seventeen members, fourteen of which are appointed by the Governor and subject to Senate confirmation. Appointed members serve staggered seven-year terms. The three other members are the Commissioner of Education, chair of the advisory council of faculty senates, and the president of the Florida Student Association. Fla. Const., Art. IX, s. 7(d).

<sup>12</sup> Fla. Const., Art. IX, s. 7(d) (“The board shall operate, regulate, control...the whole university system”); s. 20.155, F.S. 2018 (“The Board of Governors...is granted rights and privileges equal to those of departments....”).

<sup>13</sup> Fla. Const., Art. IX, s. 7(d). Each BOT is composed of thirteen members. Six members are appointed by the Governor, while five are appointed by the Board of Governors. Each appointed Trustee is subject to Senate confirmation, and serve a five-year term. The remaining two members are the chair of the state university’s faculty senate and the state university’s student body president. Id.

<sup>14</sup> BOG Regulations are published on its website accessed at <https://www.flbog.edu/board/regulations/regulations.php>.

<sup>15</sup> S. 20.155(3), F.S. (All citations to Florida Statute hereafter are to the 2018 Statutes, unless otherwise noted.)

<sup>16</sup> S. 20.155(5), F.S.

<sup>17</sup> Fla. Const., Art. IX, s. 7(c), BOG Reg. 1.001.

<sup>18</sup> BOG Reg. 1.001.

<sup>19</sup> Id.

<sup>20</sup> BOG Reg. 1.001(3)(j).

<sup>21</sup> S. 1011.45, F.S.

carryforward. The starting balance of E&G carryforward funds each fiscal year is reported to the BOG with operating budgets. Actual expenditures of current and carryforward E&G funds are reported at the end of the fiscal year. Universities are expected to keep an amount equal to 5% of E&G revenues as a minimum reserve.<sup>22</sup>

Additional funding sources for university operations include revenues from contracts and grants, auxiliary enterprises, local funds and faculty practice plan funding.<sup>23</sup> Tuition and non-resident fees are both authorized and appropriated by the Legislature.

Fixed capital funding sources for universities include Public Education Capital Outlay (“PECO”) appropriations, Capital Improvement Trust Fund (“CITF”) financing, bonding, private sources including donations, and the Courtelis challenge grant program.<sup>24</sup>

#### D. Spending Regulation

E&G funds may only be expended in accordance with operating budgets approved by the BOT.<sup>25</sup> E&G funds may only be used for operating activities such as general instruction, research, public service, plant operations and maintenance, student services, libraries, administrative support and other enrollment-related and stand-alone operations.<sup>26</sup> Additionally, interest earnings on E&G funds may be used only for E&G purposes.<sup>27</sup> Universities may never spend more than the funds available.<sup>28</sup>

State appropriations may not be used for fixed capital outlay unless specifically appropriated.<sup>29</sup> Fixed capital outlay is defined in law and generally means real property and permanent fixtures and includes “repairs, and renovations to real property which materially extend its useful life or materially improve or change its functional use.”<sup>30</sup> Expenditures for plant operation and maintenance are permitted from E&G funds.<sup>31</sup> In addition, state law expressly authorizes expenditures for infrastructure serving university facilities including roads, sidewalks, sewer,

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<sup>22</sup> S. 1011.40(2), F.S.

<sup>23</sup> For FY 2018-19, non-E&G estimated revenues are approximately: \$3 billion for contracts and grants, \$2 billion for auxiliaries, \$3.1 billion in local funds and \$1.3 billion family practice revenues. BOG Reg. 9.007(3)(b)-(e) describes non-E&G operating revenues.

<sup>24</sup> See “Finance and Facilities” accessed at the BOG website at: <https://www.flbog.edu/board/office/fac/index.php>.

<sup>25</sup> See s. 1, ch. 2018-009, L.O.F. p. 42 (proviso to appropriations 15-19); s. 1011.40(2), F.S.

<sup>26</sup> BOG Reg. 9.007(3)(a)1.

<sup>27</sup> BOG Reg. 9.007(5).

<sup>28</sup> S. 1011.40(3), F.S.

<sup>29</sup> S. 216.292(5), F.S.

<sup>30</sup> S. 216.011(1)(p), F.S. Some statutory and regulatory uses of “fixed capital outlay” are broader when the context reflects that PECO appropriations may be used for repairs and renovations in addition to those.

<sup>31</sup> BOG Reg. 9.007(3)(a)1.

water, stormwater, and utility improvements.<sup>32</sup> Revenue bonds payable from non-E&G revenues may be used to fund capital projects.<sup>33</sup> However, projects financed by debt must be expressly approved by the Legislature.<sup>34</sup> Fixed capital outlay projects funded by non-appropriated funds must be approved by the Legislature if operation and maintenance of the facility will be funded from state appropriations.<sup>35</sup> Finally, a university may expend appropriated funds for fixed capital outlay projects costing less than \$1 million notwithstanding general statutory limitations.<sup>36</sup>

#### E. UCF History and Growth

In the 2018-19 school year, UCF has a student enrollment of approximately 68,000. UCF's physical plant growth has been commensurate with UCF's growth in student population. The value of UCF owned buildings after accumulated depreciation grew from \$385,303,000 in FY 2004-05 to \$838,249,000 in FY 2016-17. The sum of state capital appropriations to UCF in that same period was \$449,946,000. From 2006-07 to 2008-09, state capital appropriations peaked, averaging \$76.2 million. From 2009-10 to 2016-17, that average was \$22.8 million. Other sources of UCF capital funding, not reported here, included donations and revenue bonds financed by non-appropriated revenues. On June 30, 2017, UCF owed approximately \$125,000,000 in capital improvement debt.<sup>37</sup>

Key personnel at UCF during relevant times were:

- Dr. Dale Whittaker Provost and Executive Vice President beginning August 2014. He became UCF's fifth President, on July 1, 2018
- Dr. John C. Hitt. President for more than 26 years,<sup>38</sup> including the period in which all matters raised in the operational audit transpired.
- William Merck was Vice President for Administration and Finance for 22 years and held the additional title of Chief Financial Officer for his last 7 years with UCF.
- Tracy Clark was Associate Provost for Budget Planning and Administration and Vice President for Finance and beginning in early 2015, reported to Merck as well as to Whittaker with respect the Provost's budgetary responsibilities.
- Christy Tant was UCF Controller, reporting to Clark and Merck.

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<sup>32</sup> S. 1013.51, F.S. S. 1013.51(4) requires that university infrastructure must be authorized under s. 1013.30, F.S. governing university campus master plans.

<sup>33</sup> S. 1010.61, F.S. The statute requires the BOG to request bond issuance and lists the revenues that may be pledged, s. 1010.61(2).

<sup>34</sup> S. 1010.61(6), F.S.

<sup>35</sup> S. 1013.78, F.S.

<sup>36</sup> S. 1013.74(2)(e), F.S.

<sup>37</sup> UCF Operational Audit, Report No. 2018-153 at 36. The Report may be located at [https://flauditor.gov/pages/pdf\\_files/2019-095.pdf](https://flauditor.gov/pages/pdf_files/2019-095.pdf).

<sup>38</sup> Background information on key UCF personnel and Trustees may be found in Appendix B.

- Lee Kernek was Associate Vice President over the Facilities department, which was responsible for construction, maintenance and operational costs of UCF facilities and infrastructure. Kernek reported to Merck.
- Scott Cole became UCF General Counsel in 2002.
- Marcos Marchena, appointed by the BOG to the UCF BOT in 2011, served as Chair of the Finance and Facilities Committee from early 2014 to July 2015, when he became BOT Chair.

#### **IV. Overview of Issues**

##### **A. Expenditures of E&G Carryforward Funds for Trevor Colbourn Hall**

From August 2013 through June 2016, UCF transferred \$38 million in E&G carryforward funds from the central reserve to the Trevor Colbourn Hall Project Construction Fund.<sup>39</sup> The planning for those transfers began in 2013, although construction did not begin until 2017.<sup>40</sup>

On August 13, 2013, President Hitt authorized the allocation of \$8 million of E&G for renovation of existing Colbourn Hall.<sup>41</sup> A transfer of \$700,000 (pursuant to that allocation) was made on August 26, 2013.<sup>42</sup> A transfer of \$9.3 million was made on May 1, 2014. Two million dollars of that transfer was authorized in a meeting between a former Provost and CFO Merck increasing the original \$8 million allocation.<sup>43</sup>

In May, 2014, the BOT approved construction of TCH but did not approve the funding source.<sup>44</sup> On August 8, 2014, new Provost Dale Whittaker formally recommended that President Hitt

<sup>39</sup> UCF Operational Audit, Report No. 2019-095 at 3. This figure includes transfers for construction only. There were four additional transfers of significantly smaller amounts in 2017 and 2018 for furniture/equipment.

<sup>40</sup> Exhibit A - Planned E&G Allocations, updated as of November 15, 2013, reflecting \$8 million being allocated for FY 2013-14 with \$700,000 transferred to date. The first time it appeared on a Planned E&G Allocations list was May 22, 2013 for \$8 million.

<sup>41</sup> Exhibit B - 2013-14 E&G Budget, Summary of Allocations and Reserve, signed by President Hitt on August 13, 2013.

<sup>42</sup> Exhibit C - Christy Tant's August 22, 2013, 11:37 a.m. email to the Budget Office.

<sup>43</sup> Exhibit D - Email chain between Christy Tant, Budget Office, and Wilson Rosario on April 30, 2014.

<sup>44</sup> Construction of TCH was recommended to house the occupants of Colbourn Hall when renovation of that building began. TCH was to be comparably sized. Funding was reported to be “non-recurring” university funds. In 2016, the BOT approved a larger TCH and demolition of the old building.

approve the allocation of an additional \$18 million of E&G carryforward funds to the Colbourn Hall renovation.<sup>45</sup> Those funds were transferred to construction accounts on July 16, 2015.<sup>46</sup>

On January 20, 2015, Dr. Whittaker and President Hitt approved a plan for a combination project, involving the construction of TCH and the renovation of Colbourn Hall. That decision added \$10 million to the projected project cost. Ten million dollars of E&G carryforward funds were transferred on June 6, 2016,<sup>47</sup> bringing the total amount of E&G carryforward funds transferred for TCH construction to \$38 million.

Emails reflect that the General Counsel provided Provost Whittaker with briefing materials including BOG Reg. 9.007 upon Whittaker's arrival at UCF.<sup>48</sup> Further, Whittaker received at least one clear written explanation of the limited purposes and permissible uses of E&G funds written by Tracy Clark.<sup>49</sup> Clark reported she never briefed Whittaker about her TCH funding concerns.<sup>50</sup> Whittaker deferred to Merck's knowledge and experience and Clark deferred to Merck's authority.<sup>51</sup> All deferred to President Hitt's clear direction to build TCH despite audit concerns.

#### B. Allocation of E&G Funds for Other Capital Projects

Prior to the first transfer of E&G funds for the Colbourn projects, UCF had made two other transfers of E&G funds for other unrelated construction projects: specifically, \$75,000 was transferred on June 17, 2013 for The Venue and \$2 million was transferred on June 25, 2013 for the Facilities Surplus Showroom. Thereafter, sixteen additional transfers for various construction projects occurred between December 2014 and May 2018.<sup>52</sup>

On August 19, 2015, Provost Whittaker recommended that President Hitt approve the allocation of \$4 million of E&G funds to Phase II of the CREOL project, which had been previously allocated

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<sup>45</sup> Exhibit E - The 2014-15 E&G Budget, Summary of Allocations and Reserve document was signed by President Hitt on August 11, 2014. While the Colbourn renovation was the line on the Allocation document, the total commitment of \$28 million was primarily programmed for construction of TCH. Based on deposition testimony and documents reviewed, investigators could not determine if there was any intentional deception in using "renovation" for the allocation.

<sup>46</sup> Exhibit F - Christy Tant's June 19, 2015, 10:07 a.m. email to the Budget Office.

<sup>47</sup> Exhibit G - Email chain between William Merck, Tracy Clark, Christy Tant, and Rebeca Richards on January 20, 2015 and July 06, 2016. Christy Tant testified that she showed the last \$10 million committed as Colbourn renovation because TCH was to be constructed first, while the last funds were thought to be needed for renovation. (Tant transcript at 85.)

<sup>48</sup> Exhibit H - Scott Cole's July 24, 2014, 5:04 p.m. email to Kassema Rhue.

<sup>49</sup> Exhibit I - William Merck's December 2, 2014, 4:15 p.m. email to Tracy Clark, copying Dale Whittaker.

<sup>50</sup> BC Report at 9.

<sup>51</sup> Whittaker transcript at 14-15; Clark transcript at 49-50.

<sup>52</sup> Exhibit J - Journal Entry Summary – E&G Funding Transferred to 8 Additional Construction Projects (Prior to Funding Corrections).

by the University Budget Committee and President Hitt approved.<sup>53</sup> The \$4 million allocation was transferred on February 18, 2016.<sup>54</sup>

On August 16, 2016, the University Budget Committee met. Attached to that meeting's agenda was UCF's Central Reserve – Planned E&G Budget Allocations. That document identified \$300,000 of E&G funds being allocated to the Band Building.<sup>55</sup> On August 31, 2016, Provost Whittaker recommended President Hitt's approval of the Band Building allocation.<sup>56</sup> The \$300,000 in E&G funds were transferred on October 14, 2016.<sup>57</sup>

In addition to E&G transfers for construction of TCH, UCF transferred an additional \$46.5 million for various other capital projects, with \$13.8 million of that having been spent before the audit finding leading to this investigation. On September 18, 2018, Interim CFO Mitchell informed President Whittaker of those additional improper E&G fund transfers and the expenditures.<sup>58</sup>

On September 20, 2018, Interim CFO Mitchell presented a chart to the BOT at its meeting, disclosing three projects for which E&G funds were improperly used. UCF also identified another five projects for which E&G funds were used, but noted that the university was awaiting further clarification from the BOG as to the propriety of the use of those funds. On November 2, 2018, UCF certified to the BOG that no projects in the previous 10 years, other than TCH, had been constructed with improper funds.<sup>59</sup>

Although UCF staff and the UCF President discussed the E&G expenditures on TCH and other projects with the BOT, they did not disclose the \$32.7 million transferred but unspent. Tracy Clark testified that after providing Mitchell a list of those projects funded by the \$46.5 million, Mitchell informed her that she would only be presenting information on the \$13.8 million actually spent because that is what the president's office wanted to present.<sup>60</sup> The BOT only learned of these improper transfers through the Auditor General report. During the January 19, 2019 BOT meeting

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<sup>53</sup> Exhibit K - 2015-16 E&G Budget, Summary of Allocations and Reserve, signed by President Hitt on August 19, 2015.

<sup>54</sup> Exhibit J - Journal Entry Summary – E&G Funding Transferred to 8 Additional Construction Projects (Prior to Funding Corrections).

<sup>55</sup> Exhibit L - UCF's Central Reserve – Planned E&G Budget Allocations Fiscal 2016-17, updated August 1, 2016.

<sup>56</sup> Exhibit M - 2016-17 E&G Budget, Summary of Allocations and Reserve, signed by President Hitt on August 31, 2016.

<sup>57</sup> Exhibit J - Journal Entry Summary – E&G Funding Transferred to 8 Additional Construction Projects (Prior to Funding Corrections).

<sup>58</sup> Exhibit N - Kathy Mitchell's September 18, 2018, 5:07 p.m. email to Dale Whittaker; Mitchell transcript at 20.

<sup>59</sup> Exhibit O - Summary of Projects with E&G Cash Funding Corrections. Exhibit P - UCF's November 2, 2018 cover letter and attached BOG certification. The \$13.8 E&G expenditures on other projects were omitted as outside the BOG inquiry. See also Kathy Mitchell email to Tanya Perry dated February 8, 2019 as Exhibit Q.

<sup>60</sup> Clark transcript at 71.

Trustee David Walsh alleged that Ms. Mitchell told him that management had hoped not to have to share that information.

### C. UCF Budget and Planning Practices

#### 1. Capital Outlay Budgets Included No Funding for TCH

UCF adopts a Capital Outlay Budget each year along with its Operating Budget.<sup>61</sup> In 2016-17 through 2018-19, years in which construction of TCH occurred, the budgets showed no funding for the project.

#### 2. Inaccurate Fund Composition Reports to BOG

Universities report planned use of E&G carryforward funds to the BOG each August in a “Fund Composition Report.” UCF’s Fund Composition Reports in 2013, 2014 and 2015 listed significant amounts of E&G carryforward funds committed to “Deferred Maintenance.” Actual E&G carryforward expenditures are also reported to the BOG after each fiscal year. For those years, actual expenditure reports reflected similarly significant amounts as “Distribution and Transfers.” After the audit, UCF staff identified internal accounting records of the specific E&G carryforward transfers made for the construction projects investigated. The following table compares the noted BOG report items with the UCF accounting records of fund transfers. The table shows that the deferred maintenance commitments were sufficient to fund the construction transfers. UCF has confirmed that transfer amounts included in the table were reported to the BOG as actual expenditures as Distribution and Transfers.

Fiscal Year	Reports to Board of Governors		UCF Records of Transfers from E&G Carryforward to Construction Accounts	
	Fund Composition Report: Deferred Maintenance	Actual Expenditures Report: Distribution and Transfers	UCF Transfers for TCH Construction	UCF Transfers for Other Projects
2013-14	15,147,700	10,776,134	10,000,000	
2014-15	<sup>62</sup> 20,155,861	5,453,415		1,006,588
2015-16	12,748,600	37,185,917	28,000,000	6,820,000
2016-17	2,957,828	18,918,088		14,862,704
2017-18	2,855,114	27,740,484		21,717,000

<sup>61</sup> Copies of the FY 2016-17 through 2018-19 Capital Outlay Budgets are attached as Exhibit R.

<sup>62</sup> UCF confirmed that this sum included \$18 million committed for TCH not transferred until July 16, 2015. The \$18 million amount was also reported in the FY 2015-16 Fund Composition Report as a carryforward “Expenditure” in the current fiscal year. The funds were not actually expended until 2017 or 2018. Reporting the same E&G carryforward item in two different years illustrates that Fund Composition Reports can reflect the same university commitment in multiple years when the expenditure is either scheduled for or deferred to a subsequent year.

### 3. UCF Internal Budget Processes

#### *Budget Committees*

The University Budget Committee (“UBC”) was a university-wide Vice President level committee formed in 2015. It meets monthly to establish university-wide budget priorities and funding recommendations including uses of uncommitted E&G funds.<sup>63</sup> The TCH commitments were decided prior to formation of the UBC, by staff in weekly “budget chat” meetings called to review requests for E&G funds, including facilities needs. The Facilities Budget Committee (FBC), formed in 2017, prioritized facilities’ needs. Funding for those priorities was considered by the UBC.<sup>64</sup> As Provost, Whittaker co-chaired, hosted or sponsored all these groups. CFO Merck co-chaired the UBC.

#### *Budget Documents*

UCF staff maintained a number of budget documents to track spending plans, including the E&G Commitment list, E&G Allocation Document, and Capital Projects lists. The E&G Commitment list tracks all of the decisions of the Provost-led groups and all allocation decisions approved by the Provost.<sup>65</sup> The Provost’s approval was necessary to add a commitment to the E&G commitment list.<sup>66</sup> That list projects spending over five years and reflects the anticipated unencumbered balance in the central E&G reserve.<sup>67</sup> The E&G Allocation Document records formal allocations of E&G funds including carryforward. The Provost signs the Allocation Document, recommending it for the President’s approval.<sup>68</sup> The Capital Projects lists is an internal list of capital projects including estimated costs and funding sources. The document is divided into two sections: unfunded and funded projects.<sup>69</sup>

Additional details regarding UCF’s internal budget practices are provided in Appendix B.

### 4. Allocations of Unrealized Investment Gains

On September 6, 2018, General Counsel Scott Cole reported to the BOT that E&G funding for TCH had been refunded in part by investment earnings. But on September 20, Interim CFO Kathy

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<sup>63</sup> Clark transcript at 26.

<sup>64</sup> Clark transcript at 29.

<sup>65</sup> Clark transcript at 16.

<sup>66</sup> Tant transcript at 23.

<sup>67</sup> Clark transcript at 16-17. Central reserves include restricted funds and unrestricted funds, which are available for subsequent commitment. Restricted funds include a mandatory 5% cash reserve, specific appropriations restricted by the Legislature, and other legal encumbrances.

<sup>68</sup> Exhibit E - 2014-15 E&G Budget, Summary of Allocations and Reserve; Tant transcript at 16.

<sup>69</sup> See Exhibit S - Capital Projects Current Funding Plan, updated 03/22/16.

Mitchell reported instead that a major share of refunding came from “unrealized investment gains.”<sup>70</sup> Unrealized gains or losses represent the differences between the market value of assets and their cost. Gains and losses are “realized” when the investor sells an asset.

UCF’s transfer of unrealized gains among university accounts raised the question of how university funds in its investment program<sup>71</sup> are tracked. A September 30, 2018, spreadsheet from UCF shows 15,000 UCF accounts having an interest in \$600 million invested. Some of the accounts show a negative balance. Negative investment balances and other evidence<sup>72</sup> indicates UCF has a practice of lending assets from one account to another.

Unrealized gains share the volatility of an asset’s market price. The unrealized investment earnings assigned to E&G in September were attributable to non-E&G funds invested in securities with substantial market risk.<sup>73</sup> UCF BOT Audit Chair Bev Seay reports that securities have since been sold and equivalent gains realized. She also reports that E&G funds have been withdrawn from the UCF investment program and deposited in the SBA SPIA.<sup>74</sup>

#### D. Issues Arising During Committee Investigation

##### 1. Oversight of Carryforward Funds

BOG Regulation 9.007 prohibits inclusion of E&G carryforward funds in BOT-approved operating budgets.<sup>75</sup> Therefore, unencumbered carryforward funds may be expended without BOT direction. The BOG maintains minimal oversight of E&G carryforward budgeting through the Fund Composition Reports filed each August.

UCF annually reports expenditures of E&G carryforward funds to its BOT in combination with all E&G expenditures for the first three quarters of the fiscal year. This practice obscures significant information such as large transfers for construction projects. Additionally, transfers and

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<sup>70</sup> See September 20, 2018 UCF BOT meeting.

<sup>71</sup> As of June 30, 2018, UCF had \$329,002,144 in the State Board of Administration, Special Purpose Investment Account and \$276,810,124 in a Structured Investment Portfolio, which included more than \$91 million in equity investments. The Structured Investment Portfolio is managed pursuant to the UCF Investment Policy and Manual, a copy of which is available in the Committee office.

<sup>72</sup> See <https://thefloridachannel.org/videos/10317-florida-board-governors-workshop-part-2/>.

<sup>73</sup> Exhibit T - Structured Portfolio Realized/Unrealized Gain & Losses (2014-2018). BNY Mellon account statements provided by UCF verify that gains allocated to refunding E&G construction expenditures came from equity investments in Pools III and IV funds established under the UCF Investment Policy and Manual. Copies of the BNY Mellon statements may be reviewed at the Committee office.

<sup>74</sup> The State Board of Administration, Special Purpose Investment Account, managed for the benefit of state universities and other public entities.

<sup>75</sup> BOG Reg. 9.007(3)(a).

expenditures in the fourth quarter are not included in annual operating budget documents.<sup>76</sup> \$19.3 million in TCH transfers occurred in the fourth quarter of a fiscal year without BOT review.

University reports of actual E&G carryforward expenditures after the fiscal year use spending categories that may obscure the nature of some expenditures.

## 2. Operating Budgets

The UCF operating budgets reviewed and approved by the BOT list only revenues and do not specify any expenditures.<sup>77</sup> Administrators submit a more complete budget to the BOG that includes both revenues and expenditures. Tim Jones, BOG Vice-Chancellor, Finance/Administration and CFO, advised that this was the normal practice for all universities.

The BOG ultimately approves the operating budget for the entire SUS. The FY 2018-19 BOG-approved expenditure budget for UCF E&G funds is:<sup>78</sup>

- Salaries and Benefits \$431 million
- Expenses \$157 million
- Risk Management \$ 2.4 million
- Financial Aid \$41.3 million
- Library Resources \$ 7.1 million.

This budget offers limited information. Additional categories and specific breakdowns within each category are necessary for meaningful budget oversight.

## 3. Planning Documents

Campus Master Plans are required and regulated by law and the BOG.<sup>79</sup> Master plans serve multiple purposes including land use planning, infrastructure planning and capital improvement planning. The BOT must adopt the Master Plan. The Capital Improvements Element of the 2015-

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<sup>76</sup> Operating budgets are approved before the 4<sup>th</sup> quarter ends. Each quarter, at a Finance and Facilities Committee meeting, UCF administrators present year-to-date revenue and expenditure totals which also include total expenditures budgeted. There is no specificity of expenditures, the report is for information only, and it is not presented to the BOT. At no time is an expenditure budget ratified by the BOT.

<sup>77</sup> The quarterly Operating Budgets that went before the Finance and Facilities Committee as informational items included a glossary of budget terms with brief description of each, along with expenditure categories. The budget terms include Educational & General described as funding for instructional activities and related administrative support. See Exhibit U - University Operating Budget Report Ended March 31, 2015.

<sup>78</sup> University of Central Florida, 2018-2019 Operating Budget Summary Schedule I. Above numbers are rounded and exclude the medical school. The UCF schedule can be found at pp. 25-26 of the State University System of Florida Operating Budget Summary Fiscal Year 2018-2019. The SUS Operating Budget can be found on the BOG website at: [https://www.flbog.edu/board/office/budget/docs/2018-19\\_Combined-Final-Book.pdf](https://www.flbog.edu/board/office/budget/docs/2018-19_Combined-Final-Book.pdf).

<sup>79</sup> S. 1013.30, F.S. 2018; Chapter 21, BOG Regulations.

25 UCF Master Plan identifies funding sources, not including E&G, used for capital projects.<sup>80</sup> If the budgeting and planning for TCH had conformed to the Master Plan, E&G funds would not have been used.

The Master Plan includes a Capital Improvements List projecting fixed capital outlay projects over the 10 years of the Plan. That list includes expected funding sources<sup>81</sup> and is the basis for 5-year Capital Improvement Plans. The 2015-2025 UCF Master Plan did not incorporate a late 2014 amendment to the prior plan authorizing TCH.<sup>82</sup> A January 2019 amendment changed funding sources noted for some projects in the Capital Improvements List. The BOT agenda did not provide a reason for the changes.

UCF's "Trevor Colbourn Hall Building Program" documented the university's reason for undertaking the capital project; it also notes the project's conformity with the Campus Master Plan and applicable building codes.<sup>83</sup> The document was signed by President Hitt, Provost Whittaker, CFO Merck and Lee Kernek, among others. The document provided vague information about the TCH funding source. The Building Program was not presented to the BOT or the BOG.

Plant surveys are required by law to validate a university's facilities inventory and assess space needs.<sup>84</sup> Groups that include staff from peer institutions and BOG staff conduct the surveys. An academic building like TCH may not be constructed without support in a Plant Survey. In October 2015, a Plant Survey was conducted of the UCF campus. In that survey, Colbourn Hall was determined to be a satisfactory academic facility and renovation was recommended.<sup>85</sup> However, despite the Plant Survey, less than 6 months later, UCF administrators determined that Colbourn Hall was beyond saving, and recommended its demolition.

#### 4. Compliance Roles

UCF assigns most compliance responsibilities to the office of University Audit ("UCF Audit") and the University Compliance, Ethics and Risk Office ("Compliance office"). The Compliance office has a broad mandate,<sup>86</sup> with a focus on ethics and employee behavior<sup>87</sup> rather than institutional

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<sup>80</sup> Beginning in October, 2016, UCF noted E&G funding sources on the Capital Improvements list included in Master Plan amendments. By December 2018, seven projects had been listed with an E&G funding source. Those sources were changed by amendment in January 2019.

<sup>81</sup> Ordinary funding for fixed capital outlay projects noted in the UCF Capital Improvements List include state PECO appropriations, Capital Improvement Trust Fund (CITF) financed by a fee paid by students, bonding authorized by s. 1013.71, and private donations.

<sup>82</sup> Exhibit V - 2015-25 Master Plan, Capital Improvements List.

<sup>83</sup> SS. 1011.012, 1013.30, 1013.31, 1013.61 F.S.; Ch. 21, BOG Regulations.

<sup>84</sup> S. 1013.31, F.S.

<sup>85</sup> Exhibit W - UCF 2015 Educational Plant Survey.

<sup>86</sup> "The University Compliance, Ethics, and Risk Office supports and promotes a culture of ethics, compliance, risk mitigation, and accountability. Our office provides centralized and coordinated oversight of the university's ethics, compliance, and risk mitigation efforts through the ongoing development of effective policies and procedures, education and training, monitoring, communication, risk assessment, and response to reported issues." See <https://compliance.ucf.edu/about/>.

<sup>87</sup> <https://compliance.ucf.edu/training-3/>.

compliance with laws.<sup>88</sup> The office sponsors the “IntegrityLine,” an anonymous hotline for ethics and compliance concerns hosted by a third-party contractor. The Compliance office administers a notification system to advise recipients of law and regulatory issues. Employees can elect to receive notifications of new BOG regulations or amendments thereto, but the service is purely optional.<sup>89</sup>

UCF Audit performs audit, advisory and investigative services appropriate to the needs of the university.<sup>90</sup> UCF Audit also works as a liaison with the state Auditor General.<sup>91</sup> UCF Audit receives numerous inquiries concerning the appropriate use of funds, on which they give advice or opinions.<sup>92</sup> Employees in UCF Audit do not receive training on the application of statutes and regulations pertinent to their work<sup>93</sup> other than whistleblower training, provided by the BOG.<sup>94</sup>

UCF Audit staff and the Compliance office meet regularly to share hotline and other reports or concerns received by either office so that the appropriate staff will provide an appropriate response.<sup>95</sup> At least one UCF Audit employee attends budget directors meetings for awareness of issues, to provide advice and suggest internal controls.<sup>96</sup> The UCF Audit attendee reports information gathered to all UCF Audit staff.<sup>97</sup> No one in UCF Audit is responsible for notification of new or amended statutes and regulations.

The UCF General Counsel may advise affected departments when a proposed change in law or regulations may affect them. In the case of a significant change, attorneys may send out a memo in lieu of an email to the department head.<sup>98</sup>

UCF does not appear to require notifications or other reminders to responsible officers to ensure compliance with the laws or notice of law changes. It does not appear that UCF Audit, the Compliance office or the General Counsel’s office received any report, complaint or question relating to the misuse of E&G funds for facilities construction prior to publication of the TCH

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<sup>88</sup> BOG regulations and the “UCF General Counsel – Legal Issues” are listed among many ethics and compliance resources at <https://compliance.ucf.edu/resources/>.

<sup>89</sup> Maier transcript at 15-16.

<sup>90</sup> Maier transcript at 12-13.

<sup>91</sup> Taft transcript at 8.

<sup>92</sup> Taft transcript at 11.

<sup>93</sup> Robert Taft stated that the former chief compliance officer would provide trainings, however she left the university. He was unsure whether the current chief compliance officer provides trainings. (Taft transcript at 13-14.)

<sup>94</sup> Maier transcript at 14-15.

<sup>95</sup> Mitchell transcript at 36; Taft transcript at 40-41.

<sup>96</sup> Taft transcript at 23-24; Maier transcript at 25-26; Mitchell transcript at 32.

<sup>97</sup> Mitchell transcript at 32.

<sup>98</sup> Cole transcript at 18-19. When presented with a copy of an email received from the BOG concerning an amendment to Reg. 9.007, Cole testified that he would have waited for any of the affected departments to approach his office if they had any questions because that amendment fell squarely within Finance and Accounting. Id.

audit concerns. No internal audit previously examined E&G funds distributed to a particular department, such as Facilities.<sup>99</sup>

The BOG I.G. has investigatory responsibility for the BOG.<sup>100</sup> The House asked for an independent I.G. investigation, but Chancellor Criser declined, in part due to the limited capacity of the BOG I.G. office. UCF decided to hire an outside investigator, indicating it was unable to internally investigate the TCH misspending.<sup>101</sup> Chancellor Criser directed the BOG I.G. to monitor the Bryan Cave investigation.

### 5. BOG Guidance

University staff regularly consulted BOG accounting and facilities staff concerning BOG regulations, budgeting requirements, and BOG reporting requirements. The BOG provides little written guidance relating to university finances and capital funding. Some guidance is available on matters directly affecting Legislative Budget Requests for operating and capital outlay funds.

Laws limiting unauthorized use of funds for fixed capital outlay make an exception for university projects that cost \$1 million or less.<sup>102</sup> The BOG, however, has employed a \$2 million dollar cap on projects.

The BOB 2 list accompanying capital outlay budget requests seeks legislative authorization of facilities built with non-appropriated funds. Lee Kernek communicated that BOG staff had instructed UCF to use “E&G” as funding source on BOB 2 forms when funding sources were uncertain or unknown.<sup>103</sup> Many university BOB 2 projects have shown E&G as a funding source.<sup>104</sup> The BOG has not objected to the practice.

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<sup>99</sup> Mitchell transcript at 24.

<sup>100</sup> S. 20.055(1)-(2), F.S.; s. 1001.706(5)(f).

<sup>101</sup> If the BOG determines a BOT is “unable to address” substantiated allegations of financial mismanagement, the BOG I.G. “shall investigate,” s. 1001.706(5)(f).

<sup>102</sup> S. 1013.74(2)(e), F.S. Ambiguity remains in the definition of fixed capital outlay not including repairs and renovations to real property which do not materially extend its useful life or materially improve or change its functional use, s. 216.292(5), F.S.

<sup>103</sup> Kernek transcript at 100.

<sup>104</sup> Separate from this report, the Committee has surveyed other university’s using E&G or ambiguous funding sources on BOB 2 forms. As of this writing, results are pending and the Committee has no specific concerns about any other university or project.

## **6. Training of Employees**

UCF offered no formal training and employees learned both functions and legal requirements from job experience.<sup>105</sup> Employees had different understandings of terminology and regulations.<sup>106</sup>

## **7. Advising and Training of Trustees**

Trustees received minimal orientation and training.<sup>107</sup> However, UCF and the BOG did little to train them in the essentials of their financial responsibilities. Trustees did not understand the budget process.<sup>108</sup> Although the General Counsel received meeting agendas and materials before BOT meetings,<sup>109</sup> there was no evidence attorneys advised as to legal sufficiency of BOT matters unless specifically asked. The BOT relied on CFO Merck only to know the legitimacy of spending decisions.

## **E. Recommendations from Other Reports and Investigations**

Other reports and investigations raise issues not addressed in this report. Appendix C summarizes those issues and related recommendations.

# **V. House Investigation Activities and Discoveries**

## **A. Oversight Authority**

Legislative oversight is a fundamental check and balance. Oversight of appropriations and their possible misuse constitutes a core legislative responsibility. Committees of the Florida House have constitutional and statutory warrant to investigate any matter under their purview when the Legislature is not in session.<sup>110</sup> The Public Integrity & Ethics Committee was re-established at the 2018 Organization Session and Speaker Oliva directed Chair Tom Leek to continue the investigation Oliva initiated in September.

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<sup>105</sup> Clark transcript at 87, 120; Tant transcript at 25; Merck transcript at 115, 148; Maier transcript at 14.

<sup>106</sup> For instance, some employed in Finance and Accounting and University Audit defined carryforward as E&G carryforward, while others, such as the General Counsel and Chief Audit Executive defined it more broadly. See Tant transcript at 33, 58; Clark transcript at 53-54; Mitchell transcript at 27; Maier transcript at 38-39; Cole transcript at 57; Taft transcript at 23.

<sup>107</sup> Marchena transcript at 10-13; Merck transcript at 10-12; Clark transcript at 55-56.

<sup>108</sup> Marchena transcript at 12; Cole transcript at 41. However, Trustee Martins told Bryan Cave investigators that he had an orientation with CFO Merck and his staff when he first joined the Board to bring him up to speed on all funds and allowable uses for each. He understood that E&G funds could not be used for capital projects. (Bryan Cave Interview Notes 1.)

<sup>109</sup> Kernek transcript at 168-69.

<sup>110</sup> Fla. Const., Art. III, s. 5; s. 11.143, F.S. Such powers include authority to examine the records of any public agency and subpoena powers.

## B. Overview of Committee Investigation

UCF was at all times responsive to Committee questions and records requests. UCF cooperated with the Committee investigation. Committee staff maintained regular communication with BOG staff who were extremely cooperative and helpful.

Because multiple records requests were being submitted by the PIE Committee, the BOG and Bryan Cave, UCF made all records requested from any of the three entities available to all. UCF also provided copies of all related public records sought by other interested parties. Additionally, Bryan Cave attorneys provided documents and notes collected during witness interviews.

Committee staff reviewed thousands of documents and several audio recordings of Committee and BOT meetings.

Counsel representing former UCF employees provided copies of letters, texts, contemporaneous notes of UCF meetings and other pertinent information. The Committee also received letters delivered from the former CFO and former President, and an unsolicited call from the former CFO about the TCH matter.

Committee staff refrained from interviewing witnesses until the Bryan Cave report was published to avoid interfering with that investigation. Thereafter, the Committee deposes thirteen witnesses – former and current UCF employees and one former Trustee.<sup>111</sup> Since their depositions, some witnesses have provided supplemental information requested by the Committee.

## C. Public Hearings and Interim Reports on the Investigation

On January 22, 2019, the Committee had its first hearing on the matter under investigation. The Auditor General's Office presented the relevant audit findings and answered committee questions. The Committee Staff Director provided an initial update on the investigation.

On February 6, 2019, a second hearing included a presentation by Chancellor Criser on the BOG's response to the UCF matter.<sup>112</sup> Committee staff summarized and commented on the Bryan Cave

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<sup>111</sup> Witnesses deposed include: Former President Dale Whittaker, recently resigned BOT Chairman Marcos Marchena, General Counsel Scott Cole, Associate Dean Ronnie Korosec, Director of Budget Initiatives Lynn Gonzalez, Construction Specialist Gina Seabrook, Associate Director (University Audit) Tina Maier, Interim CFO Kathy Mitchell, Chief Audit Executive Robert Taft, former CFO William Merck, former Associate Vice President for Facilities and Safety Lee Kernek, former Associate Provost for Budget Planning and Associate Vice President for Finance Tracy Clark, and former Senior Controller Christy Tant. Transcripts of all depositions are available through the House Office of Public Records or the Committee office.

<sup>112</sup> The BOG heard a report on the Bryan Cave investigation at its meeting on January 31, 2019.

report and findings. Thereafter, the Committee approved the issuance of subpoenas to 10 witnesses for depositions and to 4 key witnesses for both depositions and Committee meeting appearances.<sup>113</sup>

## **VI. Committee Findings**

### **A. UCF Improperly Transferred as much as \$85 Million of E&G Carryforward Funds to University Construction Accounts for Unauthorized Uses**

UCF authorized \$38 million in E&G carryforward funds to be used for construction of TCH in violation of state law.<sup>114</sup> Another \$13.8 million was misspent on other projects. More than \$32.7 million of E&G carryforward funds were also transferred to construction accounts for unlawful use on other projects but remained unspent when the BOT learned of the audit findings. UCF has reported refunds of this misspending from non-E&G accounts that include investment gains earned on non-E&G funds.

### **B. UCF Administrators Failed to Disclose Promptly the Unspent E&G Transfers**

President Whittaker and UCF finance staff learned, on September 18, 2018, of the above-described \$32.7 million improperly transferred for other projects. They did not disclose those transfers to the BOT or the BOG until after audit findings, published November 27, 2018.<sup>115</sup> The Committee finds that such non-disclosure undermined transparency during the investigation.

### **C. Continuing Questions about Other Projects**

Uncertainty remains about the legitimacy of portions of the \$13.8 million spent on non-TCH projects. Assessment of these expenditures is confounded by the actions of UCF administrators in the immediate aftermath of the audit. Some refunds may have been unnecessary. Obtaining clarification prior to spending those funds would have avoided uncertainty afterward.

### **D. Unaccountable Budgeting and Spending of E&G Funds**

#### **1. BOG Reg. 9.007 Invited Unaccountable Spending of E&G Carryforward Funds.**

The BOG expressly excludes E&G carryforward funds from BOT budgetary oversight.<sup>116</sup> Without oversight, carryforward funds can become an *ad hoc* source for spending. CFO Merck and President Hitt were able to dismiss legal restrictions on E&G funds and Dr. Whittaker failed to

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<sup>113</sup> Videos of the meetings are available on the PIE Committee page at the House website.

<sup>114</sup> S. 216.292(5), F.S. 2018, BOG Reg. 9.007, s. 1013.78(1), F.S., s. 10, ch. 2017-70 LOF (p. 424-26 authorizing TCH construction with non-appropriated funds.).

<sup>115</sup> The BOT did not receive a full accounting until January 24, 2019. See January 24 Meeting Minutes beginning at p. 13. The Minutes were found on the UCF BOT website at: <https://bot.ucf.edu/files/2018/06/FinalDraft24Jan19-minutes.v5-1.pdf>.

<sup>116</sup> Reg. 9.007(4)(b).

learn about legal constraints on spending, despite responsibility to do so.<sup>117</sup> There was no routine audit or legal review, nor any legal consultation beyond the administrators involved.

## **2. Operating Budgets Do Not Comply with State Law.**

Operating budgets approved by the BOT only list expected revenues for the coming fiscal year. The Committee finds this does not comply with law requiring the BOT to adopt an operating budget including expenditures that do not exceed revenues.<sup>118</sup> The UCF BOT delegated its authority over expenditure budgets to administrators.<sup>119</sup>

## **E. Capital Budgeting and Planning Deficiencies**

Florida law and BOG regulations provide a framework of complementary capital planning and accountability components. UCF poorly implemented these components. UCF staff received inadequate training and did not understand the purpose of each planning component. As a result:

- Staff responsibilities are unclear;
- Master Plan amendments in 2014 were not incorporated into the 2015-25 Master Plan;
- The 2015 Plant Survey failed to find old Colbourn Hall deficient for academic purposes;
- The TCH Building Program did not reflect capital funding direction in the Master Plan;
- The TCH Building Program was not authorized by any UCF Capital Outlay Budget;
- The Capital Outlay Budget was not amended to authorize construction of TCH; and
- Capital Outlay Budgets did not conform to the requirements of law.<sup>120</sup>

## **F. Compliance Responsibilities**

Although UCF has compliance resources, those resources were disconnected from the budget practices leading to the misuse of E&G funds at UCF. The Committee finds:

- The UCF Office of General Counsel has not provided needed training and legal advice to Trustees on the application of BOG regulations and state law;
- UCF Audit staff has not been properly trained in pertinent laws and BOG regulations;
- UCF employees are not adequately trained to report misspending or other mismanagement to compliance offices; and
- Under President Hitt, UCF failed to foster a culture where employees with concerns about the misuse of funds could report their concerns without fear of reprisal.

## **G. BOT Members were Ill-Advised and Untrained**

In general, Trustees were unaware of their budgetary responsibility. They lacked comprehension that E&G funds were legally restricted. They relied on CFO Merck to advise them, leaving them

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<sup>117</sup> Dr. Whittaker had access to all the information available to the BOT described in Section G. of this Report.

<sup>118</sup> S. 1011.40(2), F.S. See also BOG Reg. 1.001(6)(a).

<sup>119</sup> In 2017, the UCF BOT adopted a limitation on delegation to the President requiring BOT approval of any contract or project in excess of \$2 million. But approval of specific expenditures is no substitute for institutional budgeting.

<sup>120</sup> SS. 1011.012, 1013.61, F.S.

unable to exercise oversight of multiple decisions to commit E&G funds to construction projects. Meeting agendas created by the President's office and reviewed by the General Counsel's office were not reviewed for compliance with pertinent laws.

BOT members each year received budget information that might have triggered interest in the restrictions on or actual uses of E&G funds:

- Operating budgets set out revenues by funding type but no expenditures;
- Finance and Facilities Committee members received quarterly budget information describing the authorized uses of various fund types including E&G;
- The full BOT received third quarter actual expenditure reports that specifically noted the expenditures of carryforward funds in E&G expenditures;
- The BOT received and could have reviewed BOB 2 reports and amendments to the Master Plan, Capital Improvements List, indicating E&G funds were programmed for use on multiple projects;
- The BOT approved a Capital Outlay Budget each year that cited the statute with which, on its face, the Capital Outlay Budget did not comply; and
- BOT members received facilities construction updates and other reports showing ambiguous funding sources, but did not diligently seek to understand what funds were actually being expended.

The Committee finds that BOT members were unaware that UCF was violating state laws, but they could have and should have known more than they did. The BOT may have been misled by the Administration, but they also neglected to review information closely and failed to ask detailed questions. In combination, the dereliction of duty by UCF administrators and the laxity of oversight by BOT members created significant risks for UCF.

#### **H. Internal Allocation of University Investment Earnings was Inappropriate**

UCF had \$600 million in investments as of September 2018. The unrealized gains assigned to E&G in September were in equity investments.<sup>121</sup> The Committee finds that a principal purpose of the 5% reserve requirement is to protect against economic downturns that could suppress revenues. Equity prices often fall in advance of recessions. Accordingly, the Committee finds that proper investment of E&G funds would exclude equity investments.<sup>122</sup> The purpose of public university funds, particularly operating funds, is operation of a university, not long-term investment in financial markets.

The Committee finds that allocating unrealized gains or other shares in the investment program is not a proper means of paying an internal operating obligation. The Committee further finds it questionable that a public education institution might use such a large investment fund as a source of internal financing, through transactions executed only on spreadsheets.

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<sup>121</sup> Equity investments are ownership shares such as corporate stocks or funds invested in stocks. They differ in income and risk from fixed-income investments such as corporate or government bonds.

<sup>122</sup> UCF reports it withdrew E&G funds from equity investments after auditors and Committee staff raised questions.

## **I. BOG Oversight and Support Contributed to the UCF Misspending**

The BOG has demanded accountability from UCF for its errors. However, the Committee finds the BOG does not provide sufficient guidance to university staff in matters under the BOG's jurisdiction, with the exception of those matters affecting Legislative Budget Requests. On other matters:

- Written guidance and training material are not available online;
- Written guidance solicited by university personnel is not routinely provided; and
- Reliance on oral communications can lead to inconsistent direction and misunderstanding.

The Committee acknowledges university staff may be reluctant to put sensitive inquiries in writing. Nonetheless, written inquiries and answers provide accountability and consistency.

BOG reports are not fully reviewed. Thorough review would have allowed the BOG to intervene before E&G funds were misspent. Specifically:

- BOB 2 forms showing appropriations or ambiguous funding sources should have been questioned by BOG staff;
- Fund Composition Reports with unusually large commitments like UCF's "deferred maintenance" commitments, should have been questioned by BOG staff; and
- Actual expenditure reports with anomalies such as UCF's large "Distribution and Transfers" reports should have raised questions.

The BOG failed to derive significant oversight benefit from these UCF submissions.

## **J. BOG Inspector General's Office Lacks Adequate Investigative Tools**

The BOG Inspector General's office lacks resources to exercise the robust investigative role intended by the inspector general statutes. Such resources are essential to holding universities accountable to the BOG.

## **VII. Committee Recommendations**

Based on the foregoing findings, the Public Integrity & Ethics Committee makes the following recommendations.

### **A. UCF and other Universities Should Strictly Adhere to Planning and Budget Laws**

- Capital Outlay Budgets must comply with statutory requirements showing all capital projects and the actual source of funds committed to each project.
- Capital projects in excess of \$1 million in cost should not be undertaken before the President and General Counsel certify the actual source of all funds to be expended and that planning and funding conform to the Capital Outlay Budget, Capital Improvement Plan, Master Plan, applicable laws and regulations. Such certifications should be submitted to the BOT for information at the next scheduled meeting.

- Boards of Trustees should approve Operating Budgets conforming to Florida law with some delineation of authorized expenditures, subject to revision by the BOG.
- Boards of Trustees should approve E&G carryforward commitments reported to the BOG each August and approve university changes to the approved commitments on a quarterly basis.
- E&G funds should not be transferred or encumbered except as authorized in budgets and carryforward commitment lists approved by the BOT.

#### **B. Checks and Balances Should Hold Administrators Accountable**

- Checks and balances must be instituted to ensure that no high-ranking administrator becomes a single point of both information and authority with respect to decisions involving significant sums of public funds. BOTs and the BOG should require universities to notify General Counsel, audit and compliance, and BOG staff of the substance of such decisions. Compliance staff must have authority and opportunity to question the legitimacy of such decisions.
- Capital Outlay Budgets, Fund Composition Reports and E&G carryforward expenditures should be routinely audited.
- The General Counsel, audit, and other compliance offices should help train budget, finance and accounting staff, and their administrative superiors, in applicable laws and regulations.
- Internal auditors should prioritize audits of E&G carryforward distributions and capital project funding.

#### **C. Training of Trustees and University Staff**

- Trustees should be trained in their constitutional and fiduciary responsibilities.
- General Counsels should train Trustees in their budgetary and financial responsibilities.
- General Counsel, internal audit, and compliance offices should help train all responsible university administrators in applicable laws and regulations.
- Budget and finance decision makers should receive regular notifications of changes in applicable laws and regulations including new BOG guidance.

#### **D. BOG Regulatory, Guidance and Enforcement Reform**

- The BOG should provide standards for operating budgets and capital outlay budgets consistent with the above recommendations to verify that the laws are faithfully executed.
- The BOG should provide clear guidance for Capital Improvement Plans including BOB 1 and BOB 2 lists to verify the legitimate and appropriate use of each form.
- The BOG should provide or identify standards for project planning that require proper project budgeting and authorizations, particularly funding authorization in budgets approved by the BOT.

- The BOG should require BOTs regularly to review and approve E&G carryforward spending plans.
- The BOG should provide clear written guidance or opinions upon request of university staff and BOTs on all matters of regulatory significance. FAQs and training modules covering all statutory and regulatory budget and finance matters should be available to all universities. Such information should be kept current with respect to laws and regulations.
- BOG reports should accurately reflect plans or expenditures reported. Funds not legally encumbered should never be characterized as encumbered or expended. Funds committed from E&G carryforward accounts and not encumbered or expended should be reported as E&G carryforward available for any lawful use. Funds transferred to other university accounts but not expended should not be reported as expenditures.
- To remove legal uncertainty about the use of E&G for maintenance, renovation and capital renewal:
  - The BOG should abandon its \$2 million limitation on maintenance projects or clarify its statutory or regulatory basis with a legal opinion of its General Counsel or the Attorney General; and
  - The BOG should consistently define “fixed capital outlay,” “maintenance,” “capital renewal,” “deferred maintenance,” “infrastructure,” and related terms consistent with current law.

#### **E. BOT Policy Development**

- All SUS leadership should jointly search for best practices in budgeting and accountability. Each BOT should adopt policies to ensure adherence to budget and planning laws and regulations. Such policies should require:
- Adherence to the recommendations above;
- Engagement of legal counsel to certify that each budget document submitted to a BOT for approval is compliant with applicable laws and regulations;
- Regular internal operational audits to monitor compliance with such policies;
- University investment policies and accounting of investment shares of various university accounts should disclose the source and possible use of all funds commingled in investment programs. Care should be taken to avoid risking university reserves or endowments through internal allocation practices that are not fully accountable to the BOT; and
- Internal loans should be fully disclosed and audited to ensure the safety and security of all funds, particularly E&G funds.

## **F. Audit/Legal Allegation Responses**

- The BOG I.G. should investigate significant complaints or reports of possible waste, fraud and mismanagement and submit investigative findings to the BOG, the Speaker of the House and Senate President.<sup>123</sup>
- BOTs should review each state audit finding, be fully advised by legal counsel, audit staff and trained administrators of the seriousness of findings of unlawful operations or activities, and maintain regular review of institutional responses until compliance is achieved and certified by the university's chief audit executive, BOG Inspector General, or the Auditor General.
- Each SUS institution should foster a culture that respects and responds to Auditor General Audit Findings.
- The BOG should ensure that multiple whistleblower paths are available and widely publicized to maximize opportunities for Trustees, employees, students, contractors, and taxpayers to report waste, fraud, mismanagement or other violations of governing laws.
- University Audit and Compliance staff should make annual reports to the BOG I.G. summarizing their investigative activities, findings and results.
- Public universities should employ sufficient Audit and Compliance staff to protect the interests of taxpayers and students.
- The BOG should monitor compliance activities in all institutions.
- The BOG should consider adopting a policy on crisis management, providing intervention and support to institutions affected by financial mismanagement.

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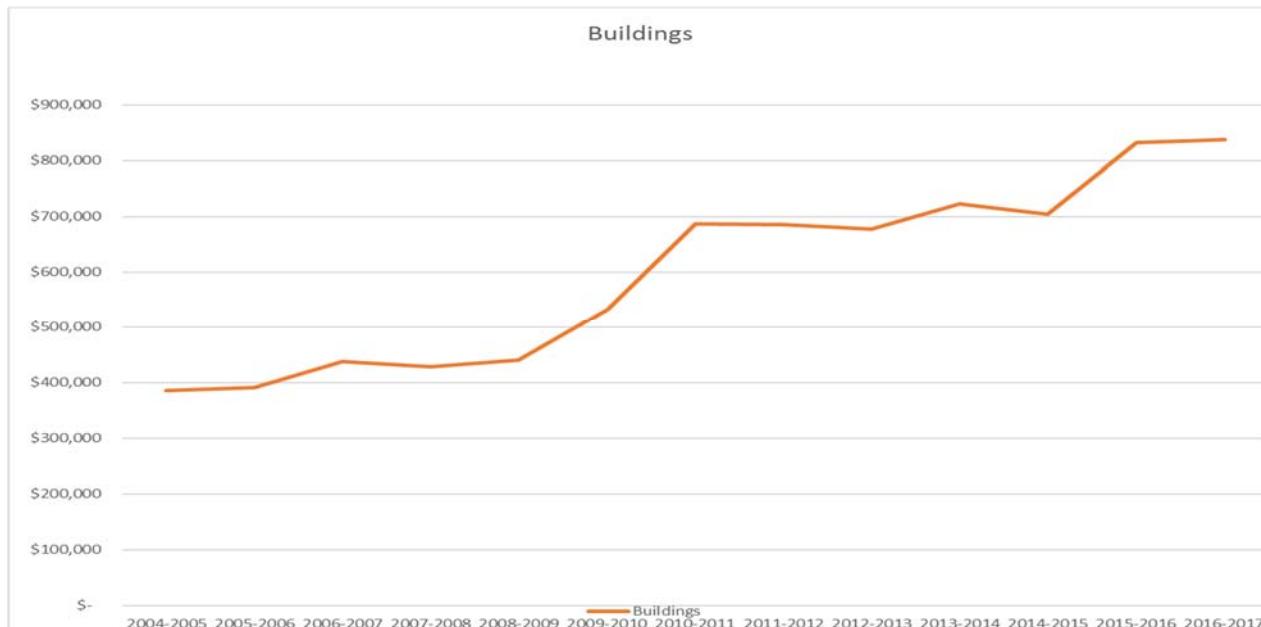
<sup>123</sup> S. 20.155(5), F.S., does not provide the BOG's Inspector General with subpoena powers. If requested by the BOG, consideration should be given to amend that section to mirror s. 14.32(5)(b), F.S.

## Appendix A – UCF Plant Growth

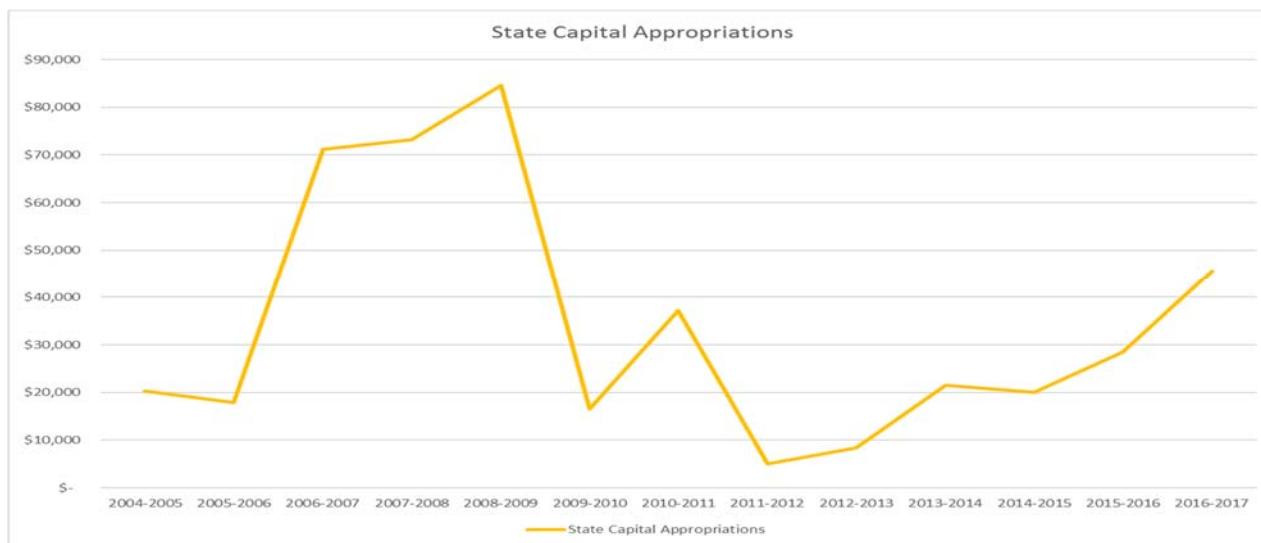
The table below lists UCF land, facilities less accumulated depreciation, construction in progress at year's end and state capital appropriations from FY 2004-05 to FY 2016-17:

Capital Assets, Net (in Thousands)	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	2014-2015	2015-2016	2016-2017
Land	\$ 9,580	\$ 9,543	\$9,685	\$9,685	\$9,685	\$ 9,685	\$ 9,685	\$ 24,822	\$ 24,822	\$ 24,822	\$ 24,822	\$ 28,133	\$ 36,159
Buildings	\$ 385,303	\$ 391,511	437,317	\$ 428,022	439,841	\$ 531,881	\$ 687,609	\$ 685,125	\$ 677,064	\$ 722,711	\$ 704,446	\$ 832,494	\$ 838,249
Construction in Progress	\$ 31,582	\$ 40,400	\$ 8,123	67,394	131,448	\$ 119,777	\$ 11,460	\$ 8,243	\$ 55,945	\$ 9,296	\$ 16,805	\$ 37,684	\$ 81,061
State Capital Appropriations	\$ 20,279	\$ 17,904	71,127	73,145	84,530	\$ 16,557	\$ 37,169	\$ 5,000	\$ 8,410	\$ 21,514	\$ 19,967	\$ 28,442	\$ 45,552

Growth of facilities value less accumulated depreciation is in this graph:



Annual state capital appropriations are shown here:



SOURCE: Financial audit reports published by the Auditor General.

## **Appendix B - UCF Internal Budget Practices**

### **UCF Budget Groups**

The following groups, made up of UCF staff and administrators, discussed the funding needs of the various UCF departments and colleges.

#### **Budget Chat Meetings**

Budget chat meetings, also known as Budget Operations Group (BOG, Jr.) meetings began at UCF some time before Provost Whittaker's arrival, but continued into his tenure as Provost. The Provost hosted these meetings, which involved his or her support staff, along with the CFO and his or her support staff.<sup>1</sup> Provost Whittaker began attending those meetings in the first weeks of his tenure as Provost.

The budget chat group met weekly and discussed all requests for funding from uncommitted E&G recurring funds as well as E&G carryforward funds, including capital funding requests. Most final decisions appear to have been officially made by the Provost or recommended by the group to the President. The E&G Commitment List was a staple in budget chats – it tracked all of the decisions made by the provost, including allocation decisions from the central reserve.<sup>2</sup>

At the budget chat meetings, new budget processes developed under Provost Whittaker's leadership were discussed, including the resurrection of the University Budget Committee.<sup>3</sup>

#### **University Budget Committee**

The University Budget Committee (UBC) was a university-wide Vice President level committee that established university-wide budget priorities and funding recommendations.<sup>4</sup> Such committee had existed some years prior to Provost Whittaker joining the university, but had stopped functioning when state funding dropped dramatically after the 2008-09 recession. Provost Whittaker resurrected the UBC in September 2014 and the Committee had its first meeting in November 2014. Provost Whittaker and VP of Administration and Finance, Bill Merck, co-chaired it. The UBC met monthly. General Counsel Scott Cole was a member,<sup>5</sup> having been added to the Committee approximately one year after its reestablishment.<sup>6</sup>

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<sup>1</sup> Clark transcript at 15.

<sup>2</sup> Clark transcript at 16.

<sup>3</sup> Clark transcript at 25.

<sup>4</sup> Clark transcript at 26.

<sup>5</sup> Cole transcript at 56.

<sup>6</sup> Clark transcript at 126.

## Appendix B - UCF Internal Budget Practices-Page 2

The UBC prioritized and budgeted uncommitted E&G funds.<sup>7</sup> This established a Vice Presidential collaborative to make decisions and recommendations formerly made by the budget chat group.<sup>8</sup>

The UBC was actively involved in an allocation of \$4 million of E&G funds for the CREOL construction project.<sup>9</sup> The UBC also regularly reviewed a version of the Capital Projects List<sup>10</sup> that reflected prior commitments of E&G and other specified funds to numerous fixed capital projects months and years prior to the encumbrance and expenditure of such funds.

### Facilities Budget Committee

The Facilities Budget Committee (FBC) was formed in December 2016 with its first meeting occurring in February 2017. Tracy Clark, Associate Provost for Budget Planning and Administration and Associate Vice President for Finance, presented the idea to Provost Whittaker because the university lacked a process under which prioritization of facilities needs could be discussed university-wide. Provost Whittaker had become familiar with a similar committee while employed at Purdue and thought this could be an effective process.<sup>11</sup>

In their appointment letters, new members were told that the FBC “will ensure the proper planning for major construction, renovation, and deferred maintenance projects and is central to the successful operation of our university.” New members were also told that the FBC “is an advisory committee for the VP of Administration and Finance and Provost to provide recommendations concerning investments in capital projects that advance the goals and mission of the university. The Committee shall review the University’s proposed capital budget and develop recommendations regarding the priority use of funding for major additions, repairs and renovations.” Accordingly, the FBC reviewed and made recommendations regarding the 5-year Capital Improvement Plan submitted to the BOT for approval each budget cycle.

The Executive Sponsors or co-chairs of the FBC were Provost Dale Whittaker and VP of Administration and Finance Bill Merck. The FBC met on a monthly basis. In August 2017, General Counsel Scott Cole became a member.

The FBC’s project priorities appear to have been subject to UBC decisions regarding actual funding commitments. The FBC reviewed versions of the Capital Projects List that identified funding sources only as “external” and “internal” sources. These broad categories hid the varieties of internal funding sources, which included E&G funds, verifying that the FBC did not commit particular funds to projects but left such decisions to the UBC.

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<sup>7</sup> Clark transcript at 75.

<sup>8</sup> Clark transcript at 27.

<sup>9</sup> Clark transcript at 74.

<sup>10</sup> See Exhibit S - Capital Projects Current Funding Plan, updated 03/22/16.

<sup>11</sup> Clark transcript at 27.

**Carryforward Budget Documents**

The following documents are found to be relevant to the planning and budgeting relevant to this investigation.

**Capital Projects List**

The Capital Projects list is an internal list of capital projects, along with estimated project costs and funding sources. The document is divided into two sections: unfunded and funded projects.<sup>12</sup>

**E&G Commitment List**

The E&G Commitment list was a staple in budget chat meetings. This internal document tracks all of the decisions the provost made and all of the allocation decisions the provost approved in budget chat meetings.<sup>13</sup> The provost's approval is necessary to add a commitment to the E&G commitment list.<sup>14</sup> It projects out five years and reflects the anticipated balance in the central reserve so that one can readily see what E&G funds are available.<sup>15,16</sup> Because the E&G commitment list was continually updated, it was more current than the E&G allocation document, which was current only on the date it was signed, ordinarily in August.<sup>17</sup>

**E&G Allocation Document**

The E&G Budget, Summary of Allocations and Reserve allocates E&G funds to specified needs across the divisions of the university. This document identifies beginning of the year permanent allocations of recurring funds as well as temporary or one-time allocations, and non-recurring allocations of E&G carryforward funds and one time appropriations. It also documents the composition of the central reserve.<sup>18</sup> The Provost signs it, recommending it for approval of the President, who also signs it.<sup>19</sup>

Because the BOT does not budget specified E&G expenditures, the E&G Allocation document appears to constitute UCF's formal annual budget of E&G funds.<sup>20</sup> Each year this document sets

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<sup>12</sup> See Exhibit S - Capital Projects Current Funding Plan, updated 03/22/16.

<sup>13</sup> Clark transcript at 16.

<sup>14</sup> Tant transcript at 23.

<sup>15</sup> Clark transcript at 16-17.

<sup>16</sup> It appears that safety, flexibility and cash flow all affect the timing of actual transfers from central E&G reserves to the various committed uses during the year. Transfers are authorized either by the Allocation document signed in August or by direct communications that the President, Provost or other budget authority has approved a commitment.

<sup>17</sup> Tant transcript at 72.

<sup>18</sup> Central reserves include restricted funds and unrestricted funds that are available for subsequent commitment. Restricted funds include a mandatory 5% cash reserve, specific appropriations restricted by the legislature, and other legal encumbrances.

<sup>19</sup> See Exhibit E - 2014-15 E&G Budget, Summary of Allocations and Reserve; Tant transcript at 16.

<sup>20</sup> Reg. 9.007(4)(b) requires operating budget information containing estimated E&G revenues and expenditures. The Allocation document should conform to expenditure budget information reported to the BOG.

## Appendix B - UCF Internal Budget Practices-Page 4

out additions or reductions from prior year spending. The recurring expenditures of the various departments and offices in the university approved for the previous year implicitly constitute the starting point for allocations.

### Fund Composition Report

The Fund Composition Report<sup>21</sup> is a document submitted to the BOG every August.<sup>22</sup>

It provides the BOG with the university E&G carryforward beginning fund balance and reflects any expenditures to date. The report reflects a university-wide balance, combining E&G carryforward in central reserve with all E&G carryforward funds held in all departments' accounts.<sup>23</sup> It reports "commitments" to expend E&G carryforward funds at unspecified times in the future, but not necessarily during the current fiscal year. In addition to reasonable BOG oversight of such plans (which actually supplement operating budgets), its main utility appears to be assuring the Legislature that universities do not have large sums of idle cash.

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<sup>21</sup> The Fund Composition Report is not required by regulation but is an informal report on carryforward plans used by the BOG in recent years to oversee management of university reserves. The non-recurring allocations in the Allocation document should give rise to the carryforward commitments in the Fund Composition Report.

<sup>22</sup> Tant transcript at 72.

<sup>23</sup> Tant transcript at 90. See also 2012-2013 Operating Budget – Beginning Fund Balance Composition. For purposes of this report and all budget documents, UCF College of Medicine balances and commitments are segregated from the rest of the university.

## **Appendix C – Recommendations from Other Reports and Investigations**

The Bryan Cave Report recommended improvements in financial policies and procedures, staff, board and administrator training, independent oversight (particularly by the BOT), improved monitoring by the BOG, as well as more robust internal auditing. The recommendations emphasized the need to change the institutional culture in which employees aware of misspending failed to raise the issue with audit or compliance officers, the general counsel, or the BOG.<sup>1</sup>

The University has commissioned two reports to review operations in the areas of administration and finance and board/staff governance. Based on the recommendation of both Bryan Cave and one of the other reports, President Whittaker permanently separated the position of CFO from COO.

After receiving the Bryan Cave Report, UCF's BOT unanimously approved a number of changes including:

- adopting as board policy the permanent separation of the position of CFO and COO;
- directing the Office of General Counsel, Compliance Ethics and Risk Office, and Internal Audit to develop updated policies and procedures for the Board's consideration to further ensure proper use of state appropriated E&G funds;
- directing the Audit and Compliance Committee to review the existing whistleblower program and recommend how to update it and educate the university community on its availability for the Board's consideration;
- adopting, as Board policy, real time audits for all capital projects in excess of \$2 million; and
- adopting a standard agenda memorandum format.

In addition to policy changes, after receipt of the Bryan Cave Report, UCF announced the termination of four subordinates of former-CFO Merck who were believed to have failed to notify the BOT of the misspending on TCH. The BOT also stripped former CFO Merck of his remaining unpaid performance bonuses and suspended Whittaker's participation in the performance bonus program for two years. On February 19, 2019, Dr. Whittaker tendered his resignation as President. The BOT accepted in a special meeting on February 21, pending a settlement agreement under negotiation as of this writing.

BOG members have publically recognized that Trustee training is necessary. At its January 31, 2019 BOG meeting, the Board directed that the Bryan Cave investigation into other UCF capital projects continue, at the direction of Inspector General Julie Leftheris, but at the expense of UCF. That investigation remains ongoing.

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<sup>1</sup> BC Report at 50-51.